

§ 704.6

12 CFR Ch. VII (1–1–02 Edition)

subject to the requirements of §§ 704.8 and 704.9.

[62 FR 12938, Mar. 19, 1997, as amended at 63 FR 24105, May 1, 1998]

§ 704.6 Credit risk management.

(a) *Policies.* A corporate credit union must operate according to a credit risk management policy that is commensurate with the investment and lending risks and activities it undertakes. The policy must address, at a minimum:

(1) The approval process associated with credit limits;

(2) Due diligence analysis requirements;

(3) Maximum credit limits with each obligor and transaction counterparty, set as a percentage of the sum of reserves and undivided earnings and paid-in capital. In addition to addressing loans, deposits, and securities, limits with transaction counterparties must address aggregate exposures of all transactions, including, but not necessarily limited to, repurchase agreements, securities lending, and forward settlement of purchases or sales of investments; and

(4) Concentrations of credit risk (*e.g.*, industry type, sector type, and geographic).

(b) *Exemption.* The requirements of this section do not apply to instruments that are issued or fully guaranteed as to principal and interest by the U.S. government or its agencies or enterprises or are fully insured (including accumulated interest) by the National Credit Union Administration or Federal Deposit Insurance Corporation.

(c) *Concentration limits.* (1) Aggregate investments in mortgage-backed and asset-backed securities are limited to 200 percent of the sum of reserves and undivided earnings and paid-in capital for any single security or trust.

(2) Except for investments in a wholesale corporate credit union, aggregate investments in repurchase and securities lending agreements with any one counterparty are limited to 400 percent of the sum of reserves and undivided earnings and paid-in capital.

(3) Except for investments in a wholesale corporate credit union, the aggregate of all investments in non-secured obligations of any single domestic issuer is limited to 100 percent of

the sum of reserves and undivided earnings and paid-in capital.

(4) For purposes of measurement, each new credit transaction must be evaluated in terms of the corporate credit union's sum of reserves and undivided earnings and paid-in capital at the time of the transaction. A subsequent reduction in the sum of reserves and undivided earnings and paid-in capital will require a suspension of additional transactions until maturities, sales or terminations bring existing exposures within the requirements of this part.

(d) *Credit ratings.* (1) All debt instruments must have a credit rating from at least one nationally recognized statistical rating organization (NRSRO).

(2) The rating(s) must be monitored for as long as the corporate owns an instrument.

(3) At the time of purchase, asset-backed securities must be rated no lower than AAA (or equivalent), other long-term investments must be rated no lower than AA (or equivalent), and short-term investments must be rated no lower than A-1 (or equivalent).

(4) Any rated instrument that is downgraded by the NRSRO used to meet the requirements of this part at the time of purchase must be reviewed by the board or an appropriate committee within 30 calendar days of the downgrade. Instruments that fall below the minimum rating requirements of this part are subject to the requirements of § 704.10.

(e) *Reporting and documentation.* (1) A written evaluation of each credit line must be prepared at least annually and formally approved by the board or an appropriate committee. At least monthly, the board or an appropriate committee must receive a watch list of existing and/or potential credit problems and summary credit exposure reports, which demonstrate compliance with the corporate credit union's risk management policies.

(2) At a minimum, the corporate credit union must maintain:

(i) A justification for each approved credit line;

(ii) Disclosure documents, if any, for all instruments held in portfolio. Documents for an instrument that has been

National Credit Union Administration

§ 704.8

sold must be retained until completion of the next NCUA examination; and

(iii) The latest available financial reports, industry analyses, internal and external analyst evaluations, and rating agency information sufficient to support each approved credit line.

§ 704.7 Lending.

(a) *Policies.* A corporate credit union must operate according to a lending policy which addresses, at a minimum:

- (1) Loan types and limits;
- (2) Required documentation and collateral; and
- (3) Analysis and monitoring standards.

(b) *General.* Each loan or line of credit limit will be determined after analyzing the financial and operational soundness of the borrower and the ability of the borrower to repay the loan.

(c) *Loans to member credit unions.* (1) The maximum aggregate amount in unsecured loans and irrevocable lines of credit to any one member credit union, excluding pass-through and guaranteed loans from the CLF and the NCUSIF, shall not exceed 50 percent of capital or 75 percent of the sum of reserves and undivided earnings and paid-in capital, whichever is greater.

(2) The maximum aggregate amount in secured loans and irrevocable lines of credit to any one member credit union, excluding those secured by shares or marketable securities and member reverse repurchase transactions, shall not exceed 100 percent of capital or 200 percent of the sum of reserves and undivided earnings and paid-in capital, whichever is greater.

(d) *Loans to members that are not credit unions.* Any loan or irrevocable line of credit made to a member, other than a credit union or a corporate CUSO, must be made in compliance with part 723 of this chapter, governing member business loans, unless such loan or line of credit is fully guaranteed by a credit union. The aggregate amount of loans and irrevocable lines of credit to members other than credit unions and corporate CUSOs shall not exceed 15 percent of the corporate credit union's capital plus pledged shares.

(e) *Loans to non member credit unions.* A loan to a credit union that is not a member of the corporate credit union,

other than through a loan participation with another corporate credit union, is only permissible if the loan is for an overdraft related to the providing of correspondent services pursuant to § 704.12. Generally, such a loan will have a maturity of only one business day.

(f) *Loans to corporate CUSOs.* A corporate credit union may make loans and issue lines of credit to corporate CUSOs, subject to the limitations of § 704.11.

(g) *Participation loans with other corporate credit unions.* A corporate credit union is permitted to participate in a loan with another corporate credit union and must retain an interest of at least 5 percent of the face amount of the loan. The participation agreement may be executed at any time prior to, during, or after disbursement. A participating corporate credit union must exercise the same due diligence as if it were the originating corporate credit union.

(h) *Prepayment penalties.* If provided for in the loan contract, a corporate credit union is authorized to assess prepayment penalties on loans.

[62 FR 12938, Mar. 19, 1997, as amended at 64 FR 57365, Oct. 25, 1999]

§ 704.8 Asset and liability management.

(a) *Policies.* A corporate credit union must operate according to a written asset and liability management policy which addresses, at a minimum:

(1) The purpose and objectives of the corporate credit union's asset and liability activities;

(2) The tests that will be used to evaluate instruments prior to purchase;

(3) The maximum allowable percentage decline in net economic value (NEV), compared to current NEV;

(4) The minimum allowable NEV ratio;

(5) The maximum decline in net income (before reserve transfers), in percentage and dollar terms, compared to current net income;

(6) Policy limits and specific test parameters for the interest rate risk simulation tests set forth in paragraph (d) of this section; and